
BY THE U.S. GENERAL ACCOUNTING OFFICE

Report To The Secretary Of The Treasury

Selling Abandoned Merchandise: How The U.S. Customs Service Could Increase Revenues

Imported merchandise which is unclaimed after 1 year is sold at auction by the U.S. Customs Service. The expenses of handling this merchandise could be reduced and the net sale proceeds increased if Customs

- shortened the storage period to less than 1 year and
- sold the merchandise promptly at the expiration of the storage period.

Approved for release by the
Director, GAO
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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

GENERAL GOVERNMENT
DIVISION

B-211885

The Honorable Donald T. Regan
The Secretary of the Treasury

Dear Mr. Secretary:

The U.S. Customs Service eventually sells merchandise abandoned by importers. Imported merchandise unclaimed by importers after 5 working days is stored, by Customs, in public or private warehouses. Under existing law, if importers do not claim the stored merchandise after 1 year, Customs considers the merchandise abandoned and sells it at auction. Customs regulations require sale proceeds to be applied in the following order: taxes, selling expenses, storage expenses, and import duties. Surplus proceeds are deposited into the U.S. Treasury.

We evaluated Customs' program for the disposal of abandoned merchandise and found that Customs could increase its net sale proceeds by revising procedures and strengthening controls for the programs. Our review of the sale of abandoned merchandise from five auctions held in Customs' New York, Pacific, and Northeast regions showed:

- A shorter storage period would have reduced storage expenses and, consequently, increased net revenues by \$71,131 if the merchandise could have been sold 6 months sooner, or \$94,093 if it could have been sold 9 months sooner. Only about 14 percent of the entries of abandoned merchandise were claimed after the third month of storage. Legislation would have to be amended to reduce the 1 year storage period.
- Additional storage costs of \$335,870 were incurred because merchandise was not removed from storage when the 1 year storage period expired. According to Customs' regional personnel, staff shortages hindered the timely identification of stored merchandise to be auctioned.

--Additional duties of about \$8,060 could have been realized if Customs had better implemented existing procedures for collecting and disposing of proceeds from the sale of bonded merchandise (merchandise entered into a warehouse by importers and stored under bond). Customs had not always properly allocated the proceeds to duties.

Because data on the disposal of abandoned merchandise is not centralized, it was not practical to take the time and effort needed to collect the data necessary to project the effect of our findings throughout Customs. We believe, however, that implementing our recommendations would result in significant additional revenues to the Treasury. The full scope of our work is explained in appendix I.

The remainder of the report discusses our findings in greater detail.

ABANDONED MERCHANDISE

Since 1789, Customs has been collecting the revenue on imports and preventing the improper entry of goods. The documentation entitling the importer to bring goods into the country is required to be filed with Customs within 5 working days after the goods arrive. If entry documentation has not been filed within the time specified, the merchandise is considered unclaimed. Customs arranges storage at the risk and expense of the importer until the entry documentation is presented.

Unclaimed merchandise is stored at private warehouses designated by Customs or at Government facilities. If the merchandise remains unclaimed for 1 year, it is considered abandoned and is sold at auction. The Tariff Act of 1930, as amended, consolidates the legislation authorizing Customs to store unclaimed merchandise and to sell abandoned merchandise.

During fiscal year 1981, more than 4.6 million formal entries of merchandise were processed by Customs. In the same period, approximately 92,700 merchandise entries were placed in storage, and approximately 75,200 were released from storage. More than 21,000 lots ¹ were abandoned and sold at auction.

¹For auction purposes, a lot may consist of part or all of an entry.

INCREASED REVENUES WOULD RESULT
FROM A SHORTER STORAGE PERIOD

Because storage, as well as other expenses, are paid from the proceeds of the auctioned merchandise, a reduction of the storage period--and related expenses--would result in increased net revenues from the sale of abandoned merchandise. The number of entries of abandoned merchandise that would be sold instead of claimed under a shorter period is uncertain. However, in our review, only about 14 percent of the entries of stored merchandise claimed were claimed after the third month of storage.

Impact of a shorter storage
period on importers

Our analysis of stored merchandise at five Customs districts disclosed that 68 percent was claimed within 3 months of importation and that 78 percent was claimed within 6 months. Less than 5 percent was claimed during the ensuing 6 months, while about 15 percent was still unclaimed, and considered abandoned, after 1 year, as the following table shows.

<u>Customs district</u>	<u>Percentage of merchandise entries claimed within</u>			<u>Percentage</u>
	<u>3 months</u>	<u>6 months</u>	<u>12 months</u>	<u>abandoned</u>
New York Seaport	66.9	79.8	84.5	10.5
JFK International Airport	70.8	75.6	78.8	18.9
Port Newark	73.8	83.3	89.3	8.8
Boston	59.3	72.2	76.6	19.1
Los Angeles: Airport	68.5	73.0	76.7	21.9
Seaport	<u>71.4</u>	<u>81.3</u>	<u>86.9</u>	<u>10.6</u>
Average for all districts	<u>68.4</u>	<u>77.5</u>	<u>82.1</u>	<u>a/ 14.8</u>

a/Totals do not add to 100 because data were not available in about 1.5 percent of the cases reviewed, and about 1.6 percent of the entries were claimed by importers even though the 1 year period had expired.

The 1 year storage period has remained unchanged for nearly 140 years since passage of the Tariff Act of 1846. A representative of the National Association of Importers and Exporters and four brokers referred to us by Customs officials told us that importers failed to claim merchandise for the following reasons:

- they lacked the documentation required by Customs for entry,
- they were unfamiliar with Customs and carrier procedures,
- they had financial or other difficulties, or
- they no longer needed the merchandise.

In addition, the representative of the National Association of Importers and Exporters told us that importers can generally post a bond to avoid moving their merchandise to storage.

A representative of the Warehousemen's Association of New York and New Jersey supported a reduced storage period and concurred with our finding that most merchandise is claimed within the first several months of importation. A warehouse proprietor who stored about 62 percent of the abandoned merchandise we reviewed in the New York area told us that his risk of loss increased in relation to the length of storage and that a reduced storage period would lessen the potential loss.

A shorter storage period would
increase auction revenues

The Tariff Act of 1930 (19 U.S.C. 1493) mandates the expenses which must be paid from auction proceeds. Proceeds remaining after all applicable expenses are paid are considered surplus and generally returned to the Treasury.² The payment priority of the expenses is set forth in 19 CFR 127.31, as follows:

1. internal revenue taxes;
2. expenses of advertising and sale;

²An importer whose merchandise is sold maintains the right to claim the surplus generated by the sale. However, Customs records indicate that inquiries by importers after merchandise is sold are rare.

3. expenses of cartage (movement to storage) and private or Government storage and labor (if the proceeds will not satisfy these expenses fully, payment is achieved prorata);
4. duties;
5. other charges due the Government; and
6. liens.

These expenses are recovered from sale proceeds as available.

We calculated the financial impact of reducing the storage period and related costs by a 6 month and a 9 month period for each merchandise lot sold in the five auctions. We restricted our analysis of the effect of reduced storage periods on storage expenses to the expenses incurred in private warehouses because Customs regional officials told us that for the five auctions we reviewed, these warehouses, as opposed to Government warehouses, handled the bulk of the abandoned merchandise. The storage expenses that would have been claimed under the shorter storage periods compared to those claimed and the amounts recovered and unrecovered by private warehouse proprietors were as follows:

Storage Expenses Claimed, Recovered, and
Unrecovered at Private Warehouses

	<u>Claimed</u>	<u>Recovered</u>		<u>Unrecovered</u>	
		<u>Amount</u>	<u>Percent</u>	<u>Amount</u>	<u>Percent</u>
Actual	\$740,845	\$275,363	37	\$465,482	63
Reducing storage by 6 months	549,349	230,551	42	318,798	58
Reducing storage by 9 months	440,383	206,867	47	233,516	53

As shown in the table, and assuming the same amount of sale proceeds, warehouse proprietors will recover lesser amounts of storage fees under reduced storage periods. However, the percentage of claimed fees recovered increases as the storage period is reduced.

In addition, the reduced storage expenses would have permitted Customs to increase its revenues--in terms of increased recovery of expenses and duties and surplus--as follows:

Increases in Recovery of Government Expenses
and Duties and Surplus at Private Warehouses

	<u>Actual</u>	<u>Storage period reduced by</u>			
		<u>6 months</u>		<u>9 months</u>	
		<u>Amount</u>	<u>Increase</u>	<u>Amount</u>	<u>Increase</u>
Expenses:					
Cartage	\$ 33,348	\$ 35,296	\$ 1,948	\$ 36,264	\$ 2,916
Government storage and labor (note a)	352,251	358,214	5,963	362,426	10,175
Duty	71,542	79,813	8,271	84,891	13,349
Surplus (note b)	<u>162,661</u>	<u>217,610</u>	<u>54,949</u>	<u>230,314</u>	<u>67,653</u>
Totals	<u>\$619,802</u>	<u>\$690,933</u>	<u>\$71,131</u>	<u>\$713,895</u>	<u>\$94,093</u>

a/For sales from private warehouses, the New York Region erroneously recovers, as Government storage and labor, the expense of auction operations. This expense is more appropriately considered an expense of advertising and sale and should be recovered before storage expenses as is done in the Boston and Los Angeles districts.

b/Although some individual sales resulted in insufficient proceeds to cover expenses, the aggregate proceeds of all lots sold resulted in a surplus.

Our calculations are conservative. Almost all of the merchandise sold in the New York auctions and some in the other regions was not removed from storage by Customs immediately upon expiration of the 1 year period (thus incurring further storage costs). The above figures were calculated assuming that the same delays in removing merchandise from storage would occur even if shorter storage periods were in effect. Removal of merchandise immediately upon expiration of a shorter storage period would increase the figures significantly. This is discussed further in a following section of this report.

This increased revenue is based upon the storage expenses which would have been incurred for storage at private warehouses. Northeast Region personnel told us that they store most

merchandise in Government-leased facilities. Regional representatives said that if the storage period were 6 months or less, private storage facilities might not be needed because quicker turnover of merchandise could result in Government facilities having adequate storage space.

NOT PROMPTLY DISPOSING OF
MERCHANDISE REDUCES NET PROCEEDS

Approximately \$335,870 in additional storage expenses were incurred in two of the three regions we reviewed because merchandise was not removed for sale after 1 year of storage. This additional storage expense results in decreased net revenue to Customs and unrecovered storage claims by the warehouse proprietors.

For the three auctions we reviewed in the New York Region, storage expenses of approximately \$304,370 were incurred after the expiration of the storage period. These expenses represented 54 percent of total storage expenses for all of the merchandise sold in the three auctions. All lots auctioned were stored for more than a year. Ninety percent were stored 19 or more months, and nearly 50 percent were stored for more than 2 years, as the following table shows:

<u>Months in private storage</u>	<u>Number of lots</u>	<u>Percent</u>
13 - 18	95	10
19 - 24	376	42
25 - 30	241	27
Over 30	<u>188</u>	<u>21</u>
Total	<u>900</u>	<u>100</u>

The New York Region conducts about nine auctions annually and was attempting speedier disposition of stored merchandise. However, regional representatives told us that staff shortages caused delays in identifying the large amounts of unclaimed merchandise to be auctioned. They said that a new computer system to track stored merchandise was being installed and should improve this situation.

Although most merchandise in the Northeast Region appeared to be sold at the next regular auction after it was eligible for sale, storage expenses of about \$31,500 were incurred for storage periods of more than a year because the region holds only

one auction annually. Regional officials advised us that more frequent auctions would be warranted if the storage period were reduced to 6 months or less. These officials estimated that the increased costs for semiannual auctions would be minimal.

DUTY ON ABANDONED BONDED
MERCHANDISE IS NOT ALWAYS
FULLY RECOVERED

Customs does not always recover the full duty on bonded merchandise (merchandise entered into a warehouse by importers and stored under bond). This occurs because Customs does not adhere to regulations governing the priority for allocating sale proceeds.

Bonded merchandise is entered directly into a warehouse by importers where it is stored under bond. Customs maintains custody of the merchandise and the bond insures the payment of duty. The Customs Procedural-Reform Act of 1978 authorizes bonded merchandise to be stored for a maximum of 5 years. Upon expiration of the 5 year period, the merchandise, if not claimed, is considered abandoned to Customs.

When abandoned bonded merchandise is sold, the priority in which sales proceeds are allocated differs from the priority applicable to other abandoned merchandise. For bonded merchandise, Customs regulations require that duty be recovered before selling, storage, and cartage expenses are reimbursed. If the amount of duty so recovered is less than the assessed duty, the unrecovered portion is collected from the surety.

For bonded merchandise sold in the New York Region, Customs erroneously pays selling, storage, and cartage expenses before attempting to recover the duty. In addition, on items where sale proceeds were insufficient to recover the full duty, Customs officials told us that no attempt was made to collect from the sureties the unrecovered portion of the duty. As a result, \$7,246 of additional duty was unrecovered on these auctions, as the following table shows:

<u>Auction</u>	<u>Duty assessed</u>	<u>Duty recovered from sale proceeds</u>	<u>Duty unrecovered</u>
1	\$ 6,552	\$5,251	\$1,301
2	3,896	900	2,996
3	<u>3,327</u>	<u>378</u>	<u>2,949</u>
Total	<u>\$13,775</u>	<u>\$6,529</u>	<u>\$7,246</u>

Our calculations indicate that had regional personnel recovered duty consistent with the priorities prescribed by Customs regulations, all assessed duties could have been recovered from sales proceeds and there would have been no need to pursue sureties. However, the New York Region did neither. Regional representatives told us that they were unaware of what the regulations prescribed.

The Pacific Region had only one bonded item for which approximately \$814 of assessed duty was unrecovered, while the Northeast Region had no sales of bonded items with assessed duty. Regional representatives in all three regions told us that they could not recall any attempt to recover duty from a surety.

Although in the auctions we reviewed, abandoned bonded merchandise represented a small percentage of merchandise sold, this percentage might increase after October 1, 1983. On that date, the original 5 year period established by the 1978 act for all bonded merchandise then in storage expires. Consequently, it might be very important to have proper recovery procedures in effect at that time.

CONCLUSIONS

The expenses of handling unclaimed imported merchandise could be reduced and the net sales proceeds increased (1) by reducing the 1 year period that unclaimed imported merchandise must remain in Customs' custody before it is considered abandoned to the Government and (2) by selling the merchandise promptly at the expiration of the prescribed storage period. On the basis of the cost savings which would result from a shorter storage period, we believe that a 6 month period or possibly a 3 month period would be desirable. However, legislation is needed before Customs can make the storage period shorter than 1 year.

RECOMMENDATIONS

We recommend that you draft and submit legislation to:

--Amend section 491(a) of the Tariff Act of 1930 (19 U.S.C. 1491(a)) to reduce the 1 year period that unclaimed imported merchandise must remain in Customs' custody before it is considered abandoned to the Government.

We also recommend that you direct the Commissioner of Customs to (1) promptly remove from storage and sell abandoned merchandise as soon as practical after the expiration of the prescribed storage period and (2) implement existing regulations for the recovery of duties from the sale of abandoned bonded merchandise.

AGENCY COMMENTS AND OUR EVALUATION

The Department of the Treasury's Assistant Secretary (Enforcement and Operations) by letter dated July 21, 1983, (see app. II) agreed with our recommendation to reduce the 1 year period Customs must hold unclaimed merchandise before it is considered abandoned and sold at auction. However, he said that Customs should be given the flexibility to hold fewer auction sales than one per year in those cases where it is determined that fewer sales are more cost efficient. We noted that the net sale proceeds from the auctions we reviewed would have benefited from shorter--not longer--storage periods. Nevertheless, we have no objection to Customs having the flexibility to determine the most cost efficient timing of auctions.

The Assistant Secretary also agreed with our recommendations to (1) encourage the prompt removal and sale of abandoned merchandise as soon as practical after the expiration of the storage period and (2) have Customs implement existing regulations for the recovery of duties from the sale of abandoned bonded merchandise. He said he would discuss these matters with the Commissioner of Customs. The Assistant Secretary stated, however, that any attempt to collect duty shortages from sureties, in the rare cases where there may be shortages, would be too time consuming and nonproductive.

We are concerned about the Assistant Secretary's position that no attempt should be made to collect duty shortages from the sureties. It is not clear why the bonding companies should

be relieved of their obligation to cover the loss of duty. If the process of collecting from the sureties is too time consuming and nonproductive, perhaps the requirement that importers secure bonds should be re-examined.

We also proposed a legislative change to provide that duties receive a higher priority than expenses of cartage, storage, labor, and advertising and sale in allocating the proceeds from the sale of abandoned merchandise. The Assistant Secretary did not agree. He stated that there was a shortage of warehouse firms, in Philadelphia and New Orleans willing to accept unclaimed merchandise for storage because the net sales proceeds were not sufficient to cover storage expenses and that the proposed change would further discourage warehouse proprietors from storing unclaimed merchandise. We recognize the Assistant Secretary's concern; however, these two cities account for only about 6 percent of imports. None of the three regions we reviewed, which account for about 49 percent, indicated to us a shortage of warehouse proprietors willing to accept unclaimed merchandise for storage. Therefore, we do not agree that the problem is so severe as to negate the merits of our proposal.

The Assistant Secretary also suggested that the sale proceeds allocation priorities be revised to provide that the expenses of advertising and sale, and expenses of cartage (movement to storage) and private or Government storage and labor receive a higher priority than Internal Revenue taxes or duties. This proposal differs from ours in that it elevates the private interests--recovery of storage and cartage expenses--above the Government's interest in taxes and duties. The issue of which interests should be paramount is debatable.

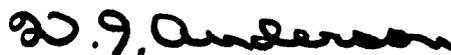
However, although the position taken by Treasury is different from ours, we believe that further discussion of the issue is not necessary at this time. As previously stated, the Assistant Secretary agreed to implement our other recommendations which will reduce the expenses of handling unclaimed merchandise and thereby benefit both the Government and the warehouse proprietors. Therefore, we are withholding our legislative proposal to elevate duty recovery to a higher priority until the results of implementing the other recommendations can be evaluated.

This report contains recommendations to you on page 10. As you know, 31 U.S.C. §720 requires the head of a Federal agency to submit a written statement on actions taken on our recommendations. This written statement must be submitted to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report. A written statement must also be submitted to the House and Senate Committees on Appropriations with an agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Director, Office of Management and Budget, and to the Chairpersons of the House and Senate Committees on Appropriations, House Committee on Government Operations, Senate Committee on Governmental Affairs, Senate Finance Committee, and House Committee on Ways and Means.

We appreciate the cooperation given our representatives during this review.

Sincerely yours,



William J. Anderson
Director

OBJECTIVES, SCOPE, AND METHODOLOGY

Our primary objective was to identify how Customs could achieve economies in disposing of abandoned merchandise. Our specific objectives were to determine whether (1) a reduction is warranted in the period unclaimed merchandise is stored before it is sold and (2) revenues are lost as a result of excessive storage periods.

Because of the decentralized nature of the auction activity, it was not practical to take the time and effort required to project the results of our findings nationwide. Therefore, a judgmental sample was selected in three of Customs' regions and selected districts within those regions--Northeast Region (Boston District); New York Region (New York Seaport Area, Newark, New Jersey, and the JFK Airport Area); and Pacific Region (Los Angeles District). Regions were selected on the basis of the magnitude of imports and auction activity, while the districts selected are the largest within the regions and represent varied modes of importation. The three regions accounted for approximately 49 percent of formal entries, nationwide, and more than 51 percent of all unclaimed merchandise in the year ended August 31, 1982.

Auctions selected for review were the June 1981 auction in the Boston District which conducts annual auctions; the September 1982 auction in the Los Angeles District which conducts quarterly auctions; and the November 1981, December 1981, and January 1982 auctions in the New York Region, which, according to regional officials, usually conducts about nine auctions annually. The auctions selected represent the latest auctions for which a final accounting had been made at the time of our fieldwork.

To determine the feasibility of a reduced storage period, we selected, at each district, a statistical random sample of merchandise entries placed into storage during fiscal year 1981. For each entry sampled, we ascertained the time elapsed between the date of importation and the date the merchandise was claimed. Our objective was to identify with 95 percent confidence the percentage of merchandise claimed within various monthly intervals. We then applied storage periods reduced by 9 months and 6 months to each sales lot of auctioned merchandise and recalculated the storage expenses, other expense, the recoveries, and surplus which would have resulted if the merchandise had been stored for these shorter periods but sold for the same amount.

We reviewed applicable laws, regulations, and procedures governing the storage and sale of unclaimed merchandise and held discussions with Customs representatives responsible for these activities. We also contacted representatives of the National Association of Importers and Exporters, Warehousemen's Association of New York and New Jersey, four brokers referred to us by Customs officials, and a warehouse operator who stored about 62 percent of the merchandise we reviewed in the New York area to discuss the feasibility of a reduction in the storage period.

Our review was made in accordance with generally accepted government auditing standards.



ASSISTANT SECRETARY

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

JUN 13 1983

Dear Mr. Anderson:

The following are comments on the draft of a proposed report entitled, "Selling Abandoned Merchandise: How the U.S. Customs Service Could Increase Revenues", which was forwarded by letter on June 13, 1983.

The first recommendation provides for a lesser time than the 1-year period which merchandise must remain in Customs custody before it is considered abandoned to the Government. We agree; however, the Commissioner of Customs should be given the flexibility to hold fewer auction sales than one per year in those cases where it is determined that fewer sales are more cost efficient.

The second recommendation would specify the priorities for allocation of proceeds from sales and the elevation of duties in the list of priorities. We disagree with this recommendation as proposed. We believe that the priority for the distribution of proceeds should be changed but that the expenses incurred in advertising, sales, cartage, storage and labor should be placed highest on the list of priorities above both Internal Revenue taxes and Customs duties. We propose that your second recommendation be changed to read: "... and (2) that among such priorities, expenses of advertising and sale; and expenses of cartage (movement to storage), private or government storage and labor shall receive a higher priority than Internal Revenue taxes or duties."

We believe the ability to obtain first class news media advertising support and professional auctioneering support would be severely compromised if those organizations were not sure of adequate payment of their expenses following a sale. This could cause major reductions in revenues from Customs auctions sales. Customs is currently experiencing a shortage in bonded warehouse firms (Philadelphia and New Orleans) willing to accept general order merchandise for storage. Again, this reluctance is due to their inability to receive adequate compensation from the government on goods stored that did not bring enough at sale to cover the storage expenses. If these proposed changes in priority were made the government would not have to pay higher storage fees than those charged regular storage customers, and there would not be a shortage in bonded warehouse firms willing to accept general order merchandise.

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The final recommendation is in order, and I will discuss with the Commissioner of Customs procedures to implement existing regulations for the recovery of duties from the sale of abandoned bonded merchandise and encourage the prompt removal and sale of abandoned merchandise as soon as practical after the expiration of the storage period.

In this regard, we believe that if we collect the duties on bonded merchandise before other charges we should not attempt to recover any duty shortages from sureties. Since the report shows that this would not have been necessary if duties were allocated first, we believe that any attempt to collect duty shortages on sureties, in the rare cases where there may be shortages, would be too time consuming and non-productive than otherwise.

We appreciate the opportunity to comment on this report and thank you for the kind remarks about the cooperation accorded your staff during this review.

Sincerely,



John M. Walker, Jr.
Assistant Secretary
(Enforcement and Operations)

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